22465

No. 22485

IN THE

United States Court of Appeals
For the Ninth Circuit

HOWARD R. KIENLE and DORA J. KIENLE, his wife,
Appellants,

v.

ALAN BOUD FLACK, an underwriter at Lloyds, London, on behalf of himself and all other Underwriters at Lloyds, London, Subscribing Certificate of Insurance No. 18201 issued by VOIGT, WALKER & CO., INC.,
Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR WESTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

HONORABLE JOHN C. BOWEN, *Judge*

BRIEF OF APPELLEE

LANE, POWELL, MOSS & MILLER
THOMAS S. ZILLY
Attorneys for Appellee

Office and Post Office Address:
1700 Washington Building
Seattle, Washington 98101
Telephone: MAin 4-1700

METROPOLITAN PRESS SEATTLE, WASH.

SUBJECT INDEX

TABLES OF AUTHORITY

Table of Cases

Textbooks

Other Authority

IN THE

United States Court of Appeals For the Ninth Circuit

HOWARD R. KIENLE and DORA J. KIENLE, his wife,
Appellants,

v.

ALAN BOUD FLACK, an underwriter at Lloyds, London, on behalf of himself and all other Underwriters at Lloyds, London, Subscribing Certificate of Insurance No. 18201 issued by VOIGT, WALKER & CO., INC.,
Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR WESTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

HONORABLE JOHN C. BOWEN, *Judge*

BRIEF OF APPELLEE

I.

JURISDICTION

Appellee accepts appellants' statement of jurisdiction and resume of the pleadings.

II.

COUNTERSTATEMENT OF THE CASE

In 1964, Pacific Farwest Mortgage & Escrow Co. (hereinafter called "Pacific Farwest"), served as escrow agent in a sale between appellants Kienle, as sellers (herein-

after called "Kienle"), and Northwestern Utilities, Inc., as purchaser (hereinafter called "Northwestern"), involving approximately eight acres of real property in Renton, Washington (Tr. 26). Kienle, as sellers, and Northwestern, as purchaser, executed a master real estate contract which provided, in part, that if Northwestern resold any of the property on contract, said contracts would be given to Kienle as additional payment toward the contract balance under the master contract (pre-trial order, admitted facts R. 56-7). The parties executed escrow instructions which required Pacific Farwest to hold the fulfillment deed until full payment had been made under the master real estate contract (Ex. A-2; R. 56).

In June, 1964, Northwestern tendered three real estate contracts (executed by Krause and Whitley and covering a resale of a portion of the property) to Kienle in full payment under the master contract; Northwestern demanded that Kienle approve these contracts and that Pacific Farwest, as escrow agent, release the fulfillment deed to Northwestern (Tr. 164). Thereafter, on July 20, 1964, Pacific Farwest received a letter from attorney Gouge, representing Kienle, notifying Pacific Farwest that under no condition was the fulfillment deed to be delivered to Northwestern without the written consent of the sellers (Ex. A-7; Finding No. 13; Tr. 163). Three days later, Kienle employed another attorney who, by letter dated July 23, 1964, also instructed Pacific Farwest that the fulfillment deed should not be delivered to Northwestern without written consent of the Kienles (Ex. A-8; Finding No. 14; Tr. 142, 146).

When Pacific Farwest received these conflicting demands, Mr. DeCrane Cooke, its president, consulted at-

torney Leslie Yates,[1] for advice (Tr. 166, 167). Yates recommended to Pacific Farwest that it file an interpleader action, as permitted under the escrow instructions, because of the conflicting demands (Ex. A-2; Tr. 149-150, 167).

Pacific Farwest, by Mr. DeCrane Cooke,[2] intentionally decided to disregard the instructions from the Kienles' attorneys, to disregard attorney Yates' advice to interplead, and to deliver the fulfillment deed to Northwestern (Tr. 167, 168, 175, 183). Cooke testified that he clearly understood there was a "distinct possibility" that Pacific Farwest would be sued in the event he released the fulfillment deed to Northwestern (Tr. 175).

Prior to delivery of the deed, and to provide protection and security in the event of litigation, Pacific Farwest obtained an indemnity agreement from Northwestern, and its individual principals, the text of which is reproduced as appendix B to this brief for the court's convenience (Ex. A-30; Tr. 170, 175, 201-203). As additional security, before it would release the deed, Pacific Farwest demanded and obtained two demand promissory notes from Northwestern, each in the amount of $1,500, one payable in the event suit should be commenced as a result of the release of the fulfullment deed and the other being payable unconditionally (Ex. A-31; Tr. 175, 180, 203-204). Pacific Farwest further demanded and obtained a mortgage from Northwestern to secure the unconditional promissory note (Tr. 176, 180).

1. Yates was the attorney who had incorporated Pacific Farwest about March 1, 1964 (Tr. 159), was a director of the escrow company and acted as counsel for the corporation. (Finding 15, R. 253; Tr. 81, 160, 166).

2. All action by Pacific Farwest, in connection with the Kienle escrow transaction, was taken by Mr. DeCrane Cooke, its president and escrow officer.

After Pacific Farwest obtained the executed indemnity agreement, two promissory notes and mortgage to secure the notes, it released the fulfillment deed from escrow on or about August 20, 1964 (Tr. 180). At about the time the deed was delivered, Northwestern paid Pacific Farwest the $1,500 pursuant to the unconditional demand note (Tr. 175). As a result of the transfer of title, and the fraud of Northwestern, the Kienles lost title to their property without receiving adequate consideration.[3]

On November 12, 1964, Kienle commenced an action in State court against Northwestern, its principal officers, and other defendants including Pacific Farwest, to quiet title, to rescind the transaction and for damages. The State court complaint (Ex. A-20; Tr. 70), alleged against Northwestern, in part, as follows:

> "That the defendant, Northwestern Utilities, Inc., and the defendant, William A. Cannon and Melvin Freimuth, on or about April 8, 1964, by means of fraudulent schemes, trick, misrepresentation, and preconceived deceit, induced the plaintiffs to enter into an Earnest Money Receipt and Agreement providing for the latters' sale of their real property hereinafter described, to the defendant, Northwestern Utilities, Inc., for the sum of $42,500.00. That said Agreement provided that the sum of $5,000.00 was to be paid down by the defendant, Northwestern Utilities, Inc., and . . . the defendants hereinabove referred to did

3. The foregoing summarizes the facts found by the trial court as Findings of Fact 5 through 20 (R. 251-254). None are challenged by appellants, except that Finding 20 should have stated Pacific Farwest knew and appreciated there was a *distinct possibility* (rather than likelihood) of being sued by the Kienles if the deed were released. It was on the basis of these facts, peculiar to this case, that the court below further found as a fact that the delivery of the deed did not constitute a negligent act, error or omission (Finding 20, R. 254), and concluded that the delivery of the deed was an intentional and wilful act not within the coverage provision of the appellee's policy of insurance (Conclusion 6, R. 261).

> not intend to pay the down payment recited in said Earnest Money Receipt and Agreement and, in fact, never did make such payment."

The complaint (Ex. A-20) alleged against Pacific Farwest, that:

> "In fact, prior to and subsequent to the transaction involving plaintiff's land, the defendant, Pacific Farwest Mortgage and Escrow Co. has been acting in collusion with the defendant, Northwestern Utilities, Inc., . . . and released the deed to Northwestern contrary to instructions."

At all times material, Pacific Farwest was insured under the Escrow Agent's Errors & Omissions policy here in question. In December, 1964, Pacific Farwest provided appellee with notice of the original Kienle complaint and tendered the defense of the action to appellee. Pacific Farwest's notice advised appellee's agent that details of the claim could be obtained from either DeCrane Cooke or Leslie Yates (Ex. 7; Tr. 21; Finding 23; R. 255). Yates forwarded the complaint and his answer prepared on behalf of Pacific Farwest to appellee's representative (Finding 23; R. 255). Appellee employed the firm of Lane, Powell, Moss & Miller to investigate the claim and by letter dated February 15, 1965 (Ex. A-22; Tr. 60), Mr. Gordon Moss, one of appellee's attorneys, advised Pacific Farwest that for the reasons stated in that letter, it was underwriters' conclusion that the claim (original complaint against Pacific Farwest charging fraud and deceit) was not insured under the Errors & Omissions policy. Appellee's attorneys closed their file and billed underwriters on or about March 15, 1965 (Tr. 39).

Meanwhile, without notice to appellee, on February 3, 1965, Kienle filed an amended complaint in the State

court action, adding new defendants and eliminating the allegation of collusion on the part of Pacific Farwest. Pacific Farwest did not advise or give notice to appellee of the amended complaint, did not forward the amended complaint to appellee, and did not tender defense of the amended complaint to appellee (Finding No. 27; R. 256 not challenged by appellants). By letter dated May 20, 1965, Mr. McCormick, one of appellants' counsel herein, wrote to appellee's attorney, Mr. Moss, advising him that the allegation against Pacific Farwest of collusion with Northwestern had been withdrawn and that an amended complaint had been filed (Ex. 5; Tr. 21). On May 24, 1965, Mr. Moss wrote a letter, a copy of which is reproduced as Appendix C to this brief, to Mr. Yates, Pacific Farwest's attorney, enclosing a copy of Mr. McCormick's letter and requesting that he be furnished (a) a copy of all relevant pleadings subsequent to the original complaint and answer, including particularly the amended complaint referred to in Mr. McCormick's letter, and (b) copies of the basic escrow documents, including the earnest money receipt and agreement, the real estate contract, and the escrow instructions (Ex. A-26; Tr. 46-47). No answer or other response was made by attorney Yates to this request and the requested pleadings, documents and information were not furnished (Tr. 54, 61, 65, 66).

The failure by Yates to respond to the request or furnish the pleadings and documents was no mere oversight. His determination not to respond was purposeful, based on his conclusion that it would be "futile" to comply with the insurer's requests because he "knew" underwriters would still deny coverage of the amended complaint and refuse to defend (Tr. 85, 94, 95).

Mr. Yates testified in part, regarding his failure to respond to Mr. Moss' request, as follows:

> "I am sure if they had given me a glimmer that they were going to come in and help in some way or participate in some way or recognize some sense of liability, that I could have been a lot more cooperative than I was there." (Tr. 94).

Based on the testimony of Yates, the trial court found as a fact that the determination of Yates not to respond to Mr. Moss' letter and furnish the pleadings and documents requested, was an intentional decision on the part of Mr. Yates (Finding 30; R. 257).

On November 3, 1965, Mr. Yates initiated a telephone conversation with Mr. Moss, counsel for appellee, to advise that the State court action had been completed and the court in an oral opinion had held Pacific Farwest liable to the Kienles (Tr. 72). Counsel for appellee again requested and Yates agreed to furnish the basic escrow documents plus the indemnity agreement. This was insurer's counsel's first notice of the existence of an indemnity agreement (Tr. 72). Yates agreed to furnish, at appellee's expense, a transcribed copy of the trial court's oral opinion, and further agreed to consult with appellee's counsel when Yates was served with proposed Findings of Fact and Conclusions of Law (Tr. 73). Mr. Moss advised Yates that underwriters might want to finance an appeal if, after review by appellee's counsel of the documents and evidence, it was counsel's recommendation that an appeal was indicated (Tr. 73).

A month later, on December 1, 1965, counsel for appellee wrote to Yates, renewing his request for the documents (Ex. A-27; Tr. 97). Yates did not furnish the

documents or comply with the requests made by appellee's counsel in the telephone conversation of November 3, 1965, and did not respond to the December 1, 1965 letter (Finding 32; R. 258).

On March 1, 1966, judgment was entered against Pacific Farwest in the State court action in the amount of $49,247.50. The findings of fact entered in the State court action were prepared by present counsel for appellants, who chose the language of the findings, which in part found Pacific Farwest "in error" and that its acts amounted to "negligence in performance of its contract of escrow," although neither the original nor amended complaint had alleged that Pacific Farwest was negligent[4] (Ex. 4; Tr. 20). At the time these findings were prepared by appellants' counsel, they had already decided that appellants were going to be "coming after Underwriters at Lloyds." (Tr. 72).

On May 18, 1966, after notice of appeal was filed by Mr. Yates, attorney for Pacific Farwest, appellee's counsel wrote a letter to Yates, soliciting advice concerning the status of the appeal, suggesting that underwriters might want their counsel to assist Yates in prosecuting an appeal and requesting the information previously requested so that he might report to underwriters and obtain instructions (Ex. A-28; Tr. 97). No response was made by Yates or Pacific Farwest to this letter (Finding 33; R. 258-9).

Appellants then commenced the instant action seeking a declaratory judgment that appellee, as insurer of Pacific

4. In his oral opinion, the State Court Judge did not state that Pacific Farwest had been negligent; rather that Judge found Pacific Farwest had breached its contract of escrow in delivering the deed in violation of instructions. (Ex. A-29, p. 6; Tr. 209).

Farwest, was obligated to pay appellants the amount of the State court judgment against Pacific Farwest. Appellee's policy insures against liability in respect to claims made against the assured "by reason of any negligent act, error or omission" committed by Pacific Farwest in its professional capacity as escrow agent (Ex. 1). The policy excludes claims "brought about or contributed to by the dishonesty of the assured or any of their employees," and contain the following express condition precedent:

> "5. The Assured shall as a condition precedent to their right to be indemnified under this Certificate give to Underwriters immediate notice in writing of any claim made upon them and further, upon request, shall give to Underwiters such information as Underwriters may reasonably request and as may be in the Assured's power. . . ."

From the evidence submitted at trial, the District court concluded that appellee was not liable to appellants herein.

III.
SUMMARY OF ARGUMENT

The District court correctly held that appellee was not liable to appellants on the following alternative grounds, each of which is sufficient to support the District court's judgment:

1. The judgment of liability entered against Pacific Farwest in the State court action was not binding on appellee-insurer. Notice to appellee and tender of defense of the original complaint was irrelevant because it alleged a claim of fraud against Pacific Farwest which was expressly excluded under appellee's policy of insurance. In addition, upon the filing of an amended complaint, the

original complaint became an abandoned pleading, did not support a claim by Kienle against Pacific Farwest and cannot be the basis of a claim against appellee. Appellee was not bound by the State court judgment based on the amended complaint because appellee was not given notice or furnished with the amended complaint, nor requested to defend the amended complaint. Appellants made no effort, and did not prove against appellee, an original case of liability on the part of Pacific Farwest to appellants. Accordingly, the District court had no alternative but to find that appellants failed to establish by a preponderance of the evidence, the liability of Pacific Farwest to the Kienles.

2. Pacific Farwest, as assured under appellee's policy, breached Condition No. 5 by intentionally failing to furnish the amended complaint when requested to do so, and by failing to furnish the documents and other information reasonably requested by appellee's counsel. The determination of the assured's counsel and director, Yates, that it would be futile to do so arrogated to himself a decision that appellee, not the assured, had the right to make under the policy. These acts constituted breaches of an express condition precedent to coverage under appellee's policy and, since appellants, as a judgment creditor, stand in the shoes of the assured, said breaches preclude appellants' recovery herein.

3. Even assuming the State court judgment of liability against Pacific Farwest is binding on appellee, it is not conclusive on the issue of policy coverage, and the finding of negligence is not binding because it was not essential to the judgment of liability. The only fact essential to the State court judgment against Pacific Farwest was that it

delivered the deed in violation of the escrow instructions. Because the judgment is not *res judicata* of policy coverage, and because the State court finding of negligence cannot be binding on appellee, the District Court could properly determine the question of policy coverage *ab initio,* without assist from the State court findings. The evidence demonstrates that the conduct of Pacific Farwest in releasing the deed, in conscious violation of the Kienles' instructions and with knowledge of the risk of suit, was a wilful decision and deliberate business gamble, and did not constitute a "negligent act, error or omission" under the escrow policy.

IV.
ARGUMENT

A. The Trial Court Correctly Held That the Judgment of Liability Entered Against Pacific Farwest in the State Court Action Was Not Binding on Appellee-Insurer; Appellants' Failure to Prove a Case of Original Liability Against Pacific Farwest Precludes Appellants' Recovery

The threshold issue on this appeal is whether or not the State court judgment of *liability* against Pacific Farwest was binding on appellee-insurer. This issue involves basic principles of *res judicata* and indemnity law, rather than insurance law. This issue is critical because if appellee was not bound by the judgment of liability against its insured, then it was incumbent upon appellants to establish that liability. However, appellants made no effort, in the court below, to prove that Pacific Farwest was legally liable to appellants.[5] The District court found that,

5. To prove liability, appellants would have had to establish that the three real estate contracts tendered to the seller (appellants) by the buyer (Northwestern) did not comply with the requirements of the master contract. However, the master contract, the three Krause and Whitley real estate contracts and the purchasers escrow instructions were not even made exhibits in the proceedings below. In addition, appellants did not offer proof of damages.

in this action, appellants did not prove that Pacific Farwest was legally liable to appellants (Finding 41; R. 259). Appellants assign error to this finding, only because "it completely presupposes that the findings and judgment of the State court action are not binding on this insurer." (App. Br. p. 65.) Thus, it is clear that appellants rely entirely on the proposition that appellee-insurer was bound by the judgment of liability entered in the State court action.

If appellants are to hold appellee bound by the State court judgment of liability, they must meet the requirements of *East v. Fields*, 42 Wn.2d 924, 259 P.2d 639 (1953):

> "The rule is that *when an insurer has notice of an action against an insured, and is tendered an opportunity to defend,* it is bound by the judgment therein upon the question of the insured's liability. 1. Freeman, judgments (5th ed.) 978, §447, 30 Am. Jur. 969, §237, and Restatement, Judgment 511, §107, 259 P.2d at 639," (Emphasis added.)

The Washington court, in *East v. Fields*, cited §107 of the Restatement of Judgments which provides that if a third person (appellants) has obtained a valid judgment in a separate action against the indemnitee (Pacific Farwest), then as between indemnitor (appellee-insurer) and indemnitee (Pacific Farwest),

> ". . . both are bound as to the existence and extent of the liability of the indemnitee, *if the indemnitee gave to the indemnitor reasonable notice of the action and requested him to defend it or to participate in the the defense.*" Id. at 511. (Emphasis added.)

Similarly, in *Crawford v. Pope & Talbot, Inc.*, 206 F.2d 784 (3rd Cir. 1953), the court said:

> "If the indemnitor was not a party to the original

> action against the indemnitee, and where he was under no duty to participate in the defense of the original action, or where, being under such a duty, he was not given reasonable notice of the action and requested to defend, neither the indemnitor nor the indemnitee is bound in subsequent litigation between them by findings made in the action." Id. at 795.

Therefore, it is necessary to review the undisputed facts of this case to determine whether appellee was given both adequate notice of the State court proceedings against Pacific Farwest and tendered the defense of that action. In this connection it is essential to distinguish between the original complaint and the amended complaint, in the state court proceedings, because the judgment of liability was predicated upon the amended complaint alone.

1. Notice and Tender of Defense of the Original Complaint Is Not Determinative of the Issue of Res Judicata.

The original State court complaint alleged that Northwestern was liable for "its fraudulent schemes, trick, misrepresentation, and preconceived deceit" and that Pacific Farwest had been acting in collusion with Northwestern. The policy of insurance expressly excludes claims "brought about or contributed to by the dishonesty of the Assured or any of their employees." (Ex. 1)

It is well established in Washington that the obligation of an insurer to defend is to be determined by the allegations of the complaint. *Town of Tieton v. Gen. Ins. Co.*, 61 Wn.2d 716, 380 P.2d 127 (1963); *Lawrence v. Northwest Cas. Co.*, 50 Wn.2d 282, 311 P.2d 670 (1967). In the *Lawrence* case, a liability insurance policy provided, in part, that assault and battery was to be deemed

an accident unless committed by or at the direction of the insured. The first complaint filed against the insured alleged assault and battery committed by the insured, and the insurer declined to defend. Thereafter, the complaint was amended to allege that the injury had been inflicted carelessly and negligently as well as wilfully and intentionally. The *Lawrence* court said:

> "The defendant's obligations to the plaintiff must be found in the pertinent provisions of the contract, which are clear and unambiguous. It undertook to 'defend any suit against the insured, alleging such injury.' . . . It is clear that the investigation of the occurrence was a matter which rested within the discretion of the defendant, and *its obligation to the plaintiff arose only when suit was brought, alleging an accident arising out of negligence, which was within the terms of the policy. The trial court correctly held that the defendant's liability did not arise until the serving of the second complaint, which had been amended to include an allegation of negligence. In cases where similar policy provisions have been construed, we have held that the insurer's liability to defend is to be determined by the allegations of the complaint filed against the insured. Globe Nav. Co. v. Maryland Cas. Co.,* 39 Wash. 299, 81 Pac. 826; *Isaacson Iron Works v. Ocean Accident & Guarantee Corp.,* 191 Wash. 221, 70 P.2d 1026. See, also, annotation in 50 A.L.R.2d 458." 311 P.2d at 672-3. (Emphasis added.)

The *Lawrence* decision clearly demonstrates that the Washington Supreme Court has held, and this court must follow the rule, that the insurer's liability to defend is to be determined by the allegations of the complaint. Appellants' suggestion that cases from other jurisdictions may afford an excellent precedent, is therefore not appropriate. The allegations against Pacific Farwest in Kienle's first complaint in State court alleged fraud, which

under appellee's policy was excluded by terms which were clear and unambiguous. The District court's second conclusion of law (R. 260) provides the original complaint did not allege a claim against Pacific Farwest within the policy coverage and that appellee was justified in declining coverage of the claim alleged in the original complaint. The allegations of Kienle's original complaint dictate this conclusion. *Appellants have not specified this conclusion as error,* and should not be heard in this court to contend that it was error.

Therefore, it must be concluded that, appellee was justified in declining coverage under the original complaint. Pacific Farwest's notice and tender of defense of the original complaint cannot be determinative of the issue of *res judicata,* and is irrelevant to the issue of whether appellee is bound by the State court judgment of liability against the assured.

The filing of an amended complaint gave rise to an entirely new claim, as between appellants and Pacific Farwest. *Lawrence v. Northwest Cas. Co.,* 50 Wn.2d 282, 311 P.2d 670 (1957); *Gen. Ins. Corp. v. Harris,* 327 S.W.2d 651 (Tex. Ct. Civ. App. 1959). The *Harris* court said:

> "In this case we shall not attempt an analysis of Hill's original petition. Upon the filing of the first amended petition the original petition became an abandoned pleading, could no longer furnish the basis of Hill's claim against Harris, and could no longer be considered in determining the nature of Hill's claim. Under the circumstances of the case it has become immaterial whether the original petition alleged facts bringing Hill's claim within the coverage of Harris' liability policy, as appellee contends in a counter-point, or whether it did not, as appellant contends in its first point on appeal. In the light of

> subsequent events the original petition is not to be considered in determining appellant's liability." 327 S.W.2d at 655.

Therefore, in order to establish that appellee was bound by the State court action, appellants were required to establish that appellee received proper notice of, and a request to defend, the amended complaint. *State Mutual Etc. Ins. Co. v. Watkins,* 181 Miss. 859, 180 So. 78 (1938).

2. Pacific Farwest Failed to Give Appellee Notice of the Amended Complaint or to Tender Appellee an Opportunity to Defend the Amended Complaint.

The District court's Finding of Fact No. 27, which is not specified as error on this appeal, is as follows:

> "The assured, Pacific Farwest Mortgage and Escrow Company, or its attorneys or representatives, did not advise or give notice to the defendant or his representatives of the amended complaint, did not forward the amended complaint to defendant or his representatives, and did not tender defense of the amended complaint to defendant or otherwise request underwriters to defend the amended complaint."

Appellants do not challenge this finding and the evidence in support of it is uncontradicted. It must accordingly be accepted by this court.

To satisfy the requirements of notice and tender of an opportunity to defend, appellants rely solely on a letter of May 20, 1965, from appellants' counsel McCormick to Mr. Moss, Exhibit 5 herein. This letter states, in part, that:

> "Since February 15, 1965, our investigation has led us to believe that your client's insured was not acting

in collusion with the defendant, Northwestern Utilities, Inc., and all parties have been served and there is on file an Amended Summons and Complaint reflecting this."

The issue presented is whether or not this letter (Ex. 5) satisfies the requirements of *East v. Fields, supra,* which requires that the person entitled to indemnity (Pacific Farwest) give reasonable notice of the action and request that the indemnitor (appellee) defend the action. There is no evidence that Pacific Farwest gave any notice to appellee; and no person ever requested appellee to defend the amended complaint. Exhibit 5 can hardly constitute such notice and tender of defense of the amended complaint so as to bind underwriters to a judgment subsequently entered.

Upon receipt of Exhibit 5, Mr. Moss wrote his letter of May 24, 1965, to Mr. Yates (Ex. A-26; Tr. 63).[6] In his letter, Mr. Moss requested all relevant pleadings subsequent to the original complaint and answer, including particularly the amended complaint. Appellants do not challenge Finding of Fact No. 27, that no answer or response was made by Yates to this request and that the pleadings, documents and information were not furnished.

It is noted that McCormick's letter of May 20, 1965 (Ex. 5), was not sent to Underwriters at Lloyd's, the insurer, or to Voigt, Walker & Co., Inc., its authorized Seattle representative. It was sent to Mr. Moss, who had closed his file and billed Underwriters some two months

6. Mr. Yates was the assured's counsel who had forwarded the original complaint to Voigt, Walker & Co., Inc. (Ex. A-21, Tr. 70); he had been originally designated by Pacific Farwest as one from whom details of the claim could be obtained (Ex. 7; Tr. 21; Finding 23; R. 255), and, of course, he would have a copy of the amended complaint.

previously, after declining coverage of the original complaint. Under these uncontroverted facts, it must be concluded that appellee did not receive proper notice and tender of defense of the amended complaint, and is not bound by the State court judgment based on that amended complaint. *East v. Fields, supra;* Restatement of Judgments §107. In Comment (e), Restatement of Judgments, §107, these requirements are amplified to show that it is not enough that the indemnitor have notice of the action against the indemnitee; he must in addition be requested to defend it. Thus the text states:

> ". . . the person entitled to indemnity must give adequate notice of the action to the indemnitor and request that he should defend it or participate in the defense. . . . The notification must contain full information about the proceeding, and normally at least the indemnitee, if requested to do so, is under a duty to give to the indemnitor what information he has concerning the nature of the claim and the evidence.
>
> "In order to bind the indemnitor in a subsequent action against him, the indemnitee is not obliged necessarily to surrender the entire control of the defense; he must, however, request the indemnitor to participate. . . .
>
> "The indemnitor is not bound by the judgment merely because he knew of the action or was a witness in it." Id. at 515-6.

The intentional determination of the assured through its attorney, Mr. Yates, not to forward the amended complaint, as requested, also is material in connection with the District court's finding that the assured breached a condition precedent to policy liability, as will be discussed hereafter in this brief. However, the failure to forward the amended complaint, and the failure of the

assured or anyone else to tender defense of it to underwriters, or even to contend that the policy covered the claim now made, must preclude the subsequent judgment on that amended complaint from having any binding effect upon appellee. This conclusion must follow because underwriters never had an opportunity to determine whether to "take over and conduct in the name of the Assured the defense or settlement" of the amended complaint, which right is expressly reserved to underwriters in the policy of insurance.

3. Appellants Failure to Prove an Original Case of Liability Against Pacific Farwest Precludes Appellants' Recovery Herein.

Because Pacific Farwest did not give appellee notice of the amended complaint or tender appellee an opportunity to defend, it was incumbent upon appellants to prove an original case of liability on the part of Pacific Farwest. *Seattle v. Saulez,* 47 Wash. 365, 92 Pac. 140 (1907); *Merriman v. Maryland Cas. Co.,* 147 Wash. 579, 266 Pac. 682 (1928). In *Merriman,* Maryland Casualty Co. issued a liability policy to one Bowman, who operated a farm. Merriman, injured by Bowman's vicious horse, obtained a default judgment against Bowman and commenced an action against the insurance company. A condition of the policy required that the assured furnish the company with a copy of any summons or process and an opportunity to defend any claim. It was undisputed that after Merriman was injured, Maryland Casualty Co. was informed of the injury and some correspondence relating to settlement occurred. However, there was no allegation that the insurance company was informed of the pendency of the action or at any time had an oppor-

tunity to defend it. The insurance company sought the right to defend upon the merits as against the plaintiff's claim that he was personally injured through the negligence of Bowman. The trial court held the injured person could maintain an action on the merits without the right on the part of the company to defend on the merits. The Washington Supreme Court reversed, saying:

> ". . . no case has been cited, and in our investigation we have discovered none, which holds that the failure of the assured to inform the company that an action has been begun, as required by the policy, enables the injured person to maintain an action on the policy after obtaining a judgment against the assured without giving to the insurance company the right to defend upon the merits as to the question of liability and the amount thereof. *The appellant had the right, at some time at least, to an opportunity to defend upon the merits and this is something that as yet it has never had.*" 266 Pac. at 683. (Emphasis added.)

Thus, it is clear that not only was it incumbent upon appellants to prove an original case of liability against Pacific Farwest, but appellee had the right to defend upon the merits, the claim of liability against Pacific Farwest.

However, in the District court, appellants did not attempt to prove an original case of liability against Pacific Farwest. Rather, appellants elected to stand on their contention of *res judicata*, and did not prove Pacific Farwest's release of the fulfillment deed from escrow was wrongful or violated their legal rights, or that Pacific Farwest was legally liable to appellants because of the release and delivery of the deed.

Pursuant to the Federal Rules of Civil Procedure, which permit the pleading of alternative positions, appellee

contended at the District court trial that (a) Pacific Farwest was legally within its rights under the escrow instructions to deliver the deed to the purchaser; and (b) that the intentional release of the deed, under all the circumstances, was an intentional business risk not covered by the escrow insurance policy here in issue. Appellee's contention that Pacific Farwest was legally within its rights under the escrow contract to deliver the deed to the purchaser, Northwestern Utilities, Inc., is supported by testimony of attorney Yates, who believed the escrow instructions had been satisfied. However, it should be noted that any determination of liability would necessarily involve a consideration of the master real estate contract between Kienle and Northwestern, the three real estate contracts between Northwestern and its purchasers (Krause and Whitley), the purchaser's escrow instructions and other documents, none of which were offered in evidence herein.

Finally, the record is void of any evidence to support appellants' contention that Pacific Farwest was not legally justified in releasing the fulfillment deed to Northwestern, despite the unilateral attempt of the sellers to prevent performance of the escrow contract by Pacific Farwest. Accordingly, the District court judge had no alternative but to find that plaintiffs (appellants herein) had failed to establish, by a preponderance of the evidence, a case of original liability against Pacific Farwest (Finding 41; R. 259).

B. Pacific Farwest's Breach of Condition Precedent No. 5 of the Policy Precludes Appellant's Recovery

1. The assured, Pacific Farwest, breached Condition No. 5 in failing to furnish the amended complaint to appellee's counsel after being requested to do so, and in failing to furnish documents and other information requested by appellee's counsel.

Condition No. 5 of the policy states:

> "The assured shall as a condition precedent to their right to be indemnified under this certificate give to Underwriters immediate notice in writing of any claim upon them and further upon request, shall give to Underwriters such information as Underwriters may reasonably require and as may be in the assured's power."

The only notice to appellee that an amended complaint had been filed was McCormick's letter to Mr. Moss on May 20, 1965 (Ex. 5). Mr. Moss immediately directed a letter to Leslie Yates, attorney for Pacific Farwest, requesting all relevant pleadings subsequent to the original complaint and answer, including particularly the amended complaint. Attorney Yates neither responded to this request nor furnished the requested documents. Yates testified that he did not respond or furnish documents because it would, in his opinion, have been "futile" to comply with the insurer's requests because "he knew" underwriters would continue to deny coverage under the policy (Tr. 85, 94, 95). The failure of attorney Yates to furnish the requested documents, and in particular the amended complaint, constituted a material breach of Condition No. 5 of the policy. As a consequence, appellee did not receive proper notice of the claim or sufficient information to evaluate the claim and determine whether

or not to exercise this right to assume the defense of the case.

It was a fundamental right of appellee, under the subject insurance contract, to determine whether or not the amended complaint should be defended by underwriters. The policy specifically provided that "underwriters, if they so desire, shall be entitled at their own expense to take over and conduct in the name of the assured the defense or settlement of any claim." It was not within the authority of appellee's attorney, Mr. Moss, and certainly not Pacific Farwest or its counsel, Mr. Yates, to make underwriters' decision. Obviously, the purpose of Mr. Moss' letter of May 24, 1965 to Mr. Yates was to obtain the amended complaint and forward it to London so that underwriters might determine whether or not to defend it. When Mr. Yates determined that "it wouldn't have accomplished anything as far as my client was concerned," to have sent the amended complaint, he prevented Mr. Flack, and other underwriters, from obtaining proper and adequate notice of the amended complaint and further prevented underwriters from exercising their policy rights to defend the suit.

Although the instant policy does not expressly contain a "suit forwarding" clause, appellee submits that, when appellee's counsel Moss requested that Yates forward the amended complaint (and other pleadings), the legal consequence was the same as if Condition 5 had expressly provided: "If suit is brought against the insured, he shall immediately forward to the company, every demand, notice, summons or other process received by him or his representative." In *Lee v. Travelers Ins. Co.*, 184 A.2d 636 (Munic. Ct. App. D.C. 1962), the court said:

> "The two requirements (notice of accident and forwarding of suit papers) have essentially the same purpose, i.e., notice to the insurer. Notice of the accident enables the insurer to make prompt investigation and prepare to defend any action that may be brought. Forwarding the suit papers gives the insurer notice that an action has been brought and enables it to properly defend." 184 A.2d at 639.

Thus, it seems clear that the forwarding of suit papers is a part of the notice to underwriters. Attorney Yates, counsel for Pacific Farwest, obviously recognized this when he forwarded the original complaint to appellee (Ex. A-21; Tr. 70). If there were any doubt about the assured's obligation to forward the amended complaint, it was removed by the specific request of appellee's counsel to Mr. Yates for the amended complaint. Clearly the amended complaint was information "reasonably required" by underwriters under Condition No. 5. How else could they determine whether to exercise their policy right to defend the suit? In addition, the assured's continuing refusal to furnish the basic escrow documents was also in direct violation of the second portion of Condition No. 5 which requires the assured to provide "information as underwriters may reasonably require and as may be in the assured's power."

2. *Pacific Farwest's breach of Condition No. 5 of appellee's insurance policy precludes appellants' recovery herein*

A review of judicial precedent completely supports the District's court Conclusion of Law No. 5 that the assured's intentional failure to furnish the amended complaint to appellee's counsel, after being requested to do so, constituted a material breach of the policy condition

and precluded recovery by appellants.

The case of *Sussman v. Am. Sur. Co.*, 345 F.2d 679 (5th Cir. 1965), supports the District court's conclusion, and is discussed at length in appellant's brief in an attempt to distinguish it. In *Sussman*, the original complaint was tendered to the insurer who declined coverage, and the defense of the action, because the complaint alleged facts excluded under the policy. An amended complaint was then filed adding a claim which was covered by the policy, but the insurer was not given notice or forwarded the suit papers. The *Sussman* insurance policy required the insured to immediately forward to the insurer every demand, notice, summons or other process received by him or his representative. Because this policy provision was breached, the *Sussman* court held for the insurer, stating that:

> "Since American Surety was neither notified of the amended complaint nor given any opportunity to participate in the defense on the merits, it cannot be required to pay Sussman the amount of the State court judgment she obtained against Mario." Id. at 680-1.

Appellants attempt to distinguish the *Sussman* case because the insurer in *Sussman* did not receive notice of the amended complaint. In contrast, an attorney (Mr. Moss) who had previously acted for the insurer was given notice that an amended complaint had been filed against Pacific Farwest. However, this distinction is not significant in light of the two separate and distinct requirements of (1) adequate and proper notice of the amended complaint *and* (2) an opportunity to defend. In contrast, in the present case, neither the amended complaint was furnished to appellee, nor was there a request by anyone

that appellee undertake the defense of the amended complaint.

The case of *Gen. Ins. Corp. v. Harris,* 327 S.W.2d 651 (Tex. Civ. App. 1959), is also closely in point. In *Harris,* Hill sued Harris, the insured, alleging wilful and wanton destruction of property. Harris tendered the defense to General Insurance Co. which declined on the alternate grounds that the policy did not cover property damages at all (but only bodily injury) and did not cover bodily injury if caused by wilful and wanton acts. Thereafter, a first amended complaint was filed which was tendered to the insurer and again rejected. Three more amended complaints were filed and the third one finally alleged bodily injuries. Harris, the insured, did not forward the last amended complaint to his insurance company. Harris settled the claim for $3,500 and sued on the policy. Condition 9 of the Harris policy required the insured to forward to the company every demand, notice, summons or other process. The *Harris* court, in giving force and effect to the condition of the policy, said:

> "It is undisputed that Harris did not send the Company copies of Hill's amended petitions in which he added new allegations asserting a claim for bodily injury.
>
> "Condition No. 9 is a very important provision in the insurance contract between the Company and Harris. The policy had not been cancelled. If Harris expected to hold the Company liable on the policy he should have complied with Condition No. 9 when Hill filed new allegations bringing suit within the coverage of the policy, thus giving the Company an opportunity to take over defense after amended petitions were filed bringing the case within policy coverage. Harris' failure to do so violated the terms of his insurance contract, and was fatal to his re-

covery from the Company in this suit." 327 S.W.2d at 657.

Similarly, in *Merriman v. Maryland Cas. Co.*, 147 Wash. 579, 266 Pac. 682 (1928), the Washington court said:

> "In the present case the respondent is basing his action upon a liability policy, which he claims was made for his benefit. The conditions of that policy, by its express terms, were that the respondent should have a right to defend any action that was brought against the assured and that the latter would furnish to the company the summons and other process that might be served upon him. It is at once apparent that the respondent cannot pick out of this insurance contract those provisions which are especially beneficial to him and disregard all other provisions." 266 Pac. 683.

We agree with appellants' contention that the general rule is that an insurer is estopped from relying on breaches of the cooperation clause occurring after the insurer has denied coverage under the policy. However, this rule has no application here because when the Amended Complaint was served and filed, as between assured and underwriters it was an entirely new claim. *Sussman v. American Surety Co.*, 345 F.2d 679 (5 Cir., 1965). This is so because the original Complaint alleged a claim of fraud excluded by the policy and there could be no estoppel or waiver arising from defendant's rightful declination of coverage of that claim.

No case cited by appellants holds that by rightfully declining defense of an excluded claim, an insurer waives breaches of policy conditions thereafter occurring when the situation has changed and an Amended Complaint (for purposes of this argument, assumed to be within policy coverage) is made against the assured.

Appellants rely primarily on two cases (discussed at pages 40-45 in their brief) which do not support their contentions. In *Lee v. Travelers Ins. Co.*, 184 A.2d 636 (Munic. Ct. App. D.C. 1962), the insurer made an investigation of the claim and carried on settlement negotiations. When suit was commenced, counsel for the insured party offered to send the insurer a copy of the suit papers, but this offer was refused. On the following day counsel for the injured party gave the insurer ten days notice that he intended to enter a default against the insured. The following language from the *Lee* decision, in holding the insurer had notice of the filing of the suit, and was afforded full opportunity to defend, clearly distinguishes that case from the present case:

> "In the present case, while it is undisputed that the insured failed to forward the suit papers to the insurer, it is also undisputed that the insurer received notice of the accident, made an investigation and carried on settlement negotiations which were broken off when an agreement could not be reached. The reasonable inference is that the insurer was well aware of the facts and legal issues involved and of the probability that suit would be filed.
>
> "When suit was filed and the insured failed to forward the suit papers, default was not taken without notice to the insurer. Appellant's counsel notified the insurer of the pending action and offered to furnish the insurer with copies of the suit papers; when this offer was refused appellant's counsel notified the insurer of the intention to take a default but at the same time offered to agree to extension of time the insurer required for filing of the suit and was afforded full opportunity to defend. It refused, taking the stand that it was not required to defend because of the failure of the insured to forward suit papers." 184 A.2d at 638.

The case of *Northwestern Mut. Ins. Co. v. Independ-*

ence Mut. Ins. Co., 319 S.W.2d 898 (St. Louis Ct. App. Mo. 1959), (App. Br. p. 43), can also be distinguished. In this latter case, the attorney for the third party subrogated insurance carrier actually forwarded the suit papers to the insurer, and fully complied with the condition precedent in the policy. In contrast, *no one* forwarded the amended complaint to appellee and no judicial precedent requires an insurer to go further than to request the insured to forward an amended complaint. In addition, appellee notes that the *Northwestern Mutual* court cites a decision from this court, which is in complete accord with appellee's position. In *Metropolitan Cas. Ins. Co. v. Colhurst*, 36 F.2d 559 (9th Cir. 1930), the insured (Harris) had an automobile liability policy requiring the insured to give written notice of accidents and to forward every summons or process to the insurance company. Colhurst, who had been injured in an accident with Harris, commenced an action in Solano County, California, which summons was immediately forwarded by Harris to his insurer. The insurer employed an attorney to defend on behalf of Harris, and he prepared and filed an answer for the insured. Thereafter, plaintiff's attorney wrote to the attorney for Harris, advising him that he had dismissed the Solano County suit and had commenced another action in Napa County, California. Harris, who was personally served in the Napa County suit did not provide a copy of the new complaint to the insurer, and permitted a default judgment to be taken against him. Suit was then commenced by Colhurst against Metropolitan Casualty Insurance Co. on the Napa County judgment. Judgment against the insurance company was reversed on appeal

because of the breach of the policy condition. This court said:

> "We do not think the letter referred to, from one attorney to the other, is a material circumstance. The important consideration was that appellant should be advised of the service of process so that it could appear in response thereto, in the assured's name, and make defense. This information the letter did not purport to give, and, until the defendant was served with process, appellant was powerless to take appropriate steps for its protection.
>
> "In that view, admittedly, because of his default in not sooner forwarding the summons and complaint, Harris, in case he had satisfied the judgment against him, could not have recovered upon the policy, and the question is whether or not, for like reasons, appellee is subject to the same liability." 36 F.2d at 561.

The *Colhurst* court, after reviewing cases from other jurisdictions, including the *Merriman* decision in Washington, concluded that the injured party was subject to the same disabilities to which the insured would be subject should he pay the judgment and seek indemnity.

The trial court also found that under Condition No. 5, appellee was entitled to be furnished with the documents and information appellee's counsel requested that Mr. Yates furnish to him (Finding 30; R. 257). The provision of Condition No. 5 that the assured shall give to underwriters such information as they may reasonably require is this policy's equivalent of a "cooperation clause." In *Hilliard v. United Pac. Cas. Ins. Co.,* 195 Wash. 478, 81 P.2d 513 (1938), the court stated with respect to the enforceability of a cooperation clause:

> "'cooperate' . . . does mean that the assured must give the insurer full, fair and frank disclosure of all

> information reasonably requested by the insurer to enable it to determine if there is a genuine defense." 81 P.2d at 516.

Requirements in liability policies for the cooperation of the insured universally have been held valid. Appleman on Insurance, §§4771, 4774. The insured cannot arbitrarily or unreasonably decline to assist in making a fair investigation or defense of a claim. *Royal Indem. Co. v. Morris,* 37 F.2d 90 (9th Cir., 1930).

There is no doubt that the assured's counsel (and director) Yates intentionally determined not to furnish the documents and information requested. These escrow documents were the basic contracts out of which Pacific Farwest's liability, if any, would arise. They were surely material and were hence reasonably requested by underwriters.

3. Condition No. 5 of the policy is a condition precedent to recovery.

As they unsuccessfully did in the court below, appellants continued to urge that the furnishing of information, including presumably the amended complaint, is not a condition precedent to the insurer's liability. This position is based upon appellants' remarkable construction of the language of Condition No. 5 and the use of the singular term "condition precedent." Appellants reached this strained result despite the fact that the requirement of giving notice and the further requirement of furnishing information both follow the introductory language of this 4-line, one-sentence paragraph that the obligations imposed are a "condition precedent to their right to be indemnified." This attempt to import an ambiguity into

Condition No. 5 of the policy should not be tolerated. In *Hamilton Tr. Service v. Auto Ins. Co.,* 39 Wn.2d 688, 237 P.2d 781 (1951), the court said:

> "We have not adopted the lines of reasoning found in the cases cited by respondent in order to determine the intent of the parties, or what they may or must have contemplated when making an insurance contract with reference to the extent of the risk coverage when it was clear that the words were used in their ordinary sense or meaning, nor when the language used was plain and unambiguous. . . . We have taken the position in such matters that a rule of construction should not be permitted to have the effect to make a plain agreement ambiguous and then construe it in favor of the insured. . . . We cannot avoid feeling as we read the cases cited by respondent that those courts have created ambiguities where none existed and have then used rules of construction to determine the intent of the parties and what they must have contemplated, thus enlarging the risk coverage of the insurance policies under consideration." 237 P.2d at 783-4.

Appellees therefore submit that the evidence fully supports the District court's finding that Pacific Farwest, by the acts of its attorney Yates, breached Condition No. 5. The breach of this condition precedent by Pacific Farwest, precludes appellant Kienles' recovery, because they stand in the shoes of the assured. In *Van Dyke v. White,* 55 Wn.2d 601, 349 P.2d 430 (1960), the court said:

> "If a party has breached a contract condition precedent, neither he nor one standing in his shoes may maintain an action on it, and prejudice or the lack of it is immaterial. Only a waiver of such breach or estoppel to assert it by the defendant can remove this fatality." 349 P.2d at 433.

Because of the assured's breaches of policy conditions, appellee had no opportunity to investigate the merits of

Kienles' amended complaint to determine whether or not it was covered under the policy and whether or not underwriters would defend the amended complaint. We are not here concerned with whether, in spite of Pacific Farwest's default, underwriters could have protected themselves, but whether Pacific Farwest (and those who stand in its shoes) forfeited its right, by violating a material condition of the policy. For as admitted by appellants, the breach of an express condition precedent will release the insurer from the obligations imposed by the insurance contract, although no prejudice may have resulted (App. Br., p. 36). *Sears, Roebuck & Co. v. Hartford Etc.*, 50 Wn.2d 443, 313 P.2d 347 (1957). Appellants cannot pick out of the subject insurance policy those provisions which are especially beneficial to them and disregard the express language of Condition No. 5 of the policy. In the *Sears, Roebuck & Co.* case, *supra,* the Washington court said:

> "Since an insurance policy is merely a written contract between an insurer and the insured, courts cannot rule out of the contract any language which the parties thereto have put into it; cannot revise the contract under the theory of construing it; and neither abstract justice nor any rule of construction can create a contract for the parties which they did not make for themselves." 313 P.2d at 350.

This court must enforce Condition No. 5 of the policy as written.

C. The Trial Court Correctly Found and Concluded That Pacific Farwest's Release and Delivery of the Fulfillment Did Not Constitute a Negligent Act, Error or Omission Within the Basic Coverage Provisions of the Policy

The question of whether the assured's act of delivering the deed constituted "a negligent act, error or omission

within the coverage of appellee's policy, is doubtless the most intellectually challenging issue in this case. However, it is an issue which this court need not decide unless the court first holds that appellee, insurer, is bound by the judgment of liability entered in the State court proceedings against the assured, and holds further that Pacific Farwest did not breach an express condition precedent of the policy. If appellants successfully hurdle these two obstacles, they must then establish that Pacific Farwest's intentional release of the deed, in violation of written demands from Kienle's attorney was conduct insured under appellee's policy covering claims arising out of a "negligent act, error or omission" committed by the assured. The District court concluded that the act of the assured in releasing the fulfillment deed from escrow, upon which the assured's liability to appellants was based in the State court action, was an intentional and wilful act and did not constitute a negligent act, error or omission within the meaning of the coverage provisions of the policy (Finding No. 20; Concl. of Law 6; R. 254, 261).

1. Even if the state court judgment of liability against Pacific Farwest is binding on underwriters, the finding of negligence is not binding because it was not essential to the judgment of liability.

The applicable Washington rule of law was established in *East v. Fields*, 42 Wn.2d 924, 259 P.2d 639 (1953). In the *Fields* case, plaintiffs brought an action to recover damages for injuries suffered in an automobile accident in Washington. Defendant Fields owned the car and had a policy of insurance which excluded coverage if the car was driven by another member of the armed forces without the insured's consent. Fields tendered the defense of

the action to his insurer, who denied coverage. Plaintiff recovered a judgment against Fields and defendant Finch, a soldier who was driving at the time of the accident. In a subsequent garnishment proceeding, in the same action, plaintiffs garnished Field's insurance company contending that a finding of fact in the main action, that Fields was in the car at the time of the accident, was *res judicata*, and therefore binding on the insurance company. The garnishee-defendant produced evidence that the defendant-owner was not in the car at the time of the accident, and accordingly the court dismissed the writ. Plaintiffs appealed to the Washington Supreme Court, presenting the issue of whether the insurance company could relitigate whether or not Fields was in the car at the time of the accident.

The Washington court set forth the following rules, controlling on this court:

> "The rule is that when an insurer has notice of an action against an insured, and is tendered an opportunity to defend, it is bound by the judgment therein upon the question of the insured's liability. 1 Freeman, Judgments (5th ed.) 978, §447; 30 Am. Jur. 969, §237; and Restatement, Judgments 511, §107. *The judgment, however, is not conclusive as to the question of coverage of the policy in question (Restatement, Judgments* 517, §107 (g)), *for the reason that the causes of action for tort liability and for indemnity liability are separate* and *distinct.* 1 Freeman, Judgments (5th ed.) 991, §450. *Thus, the judgment fixing the tort liability of the defendants in the main action is not* res judicata *of the indemnity liability of the insurance company in the garnishment proceedings.*" 259 P.2d at 639. (Emphasis added.)

Thus, it is clear, under Washington law, that the judgment fixing the liability of Pacific Farwest in the State court

action (assuming for argument that appellee is bound) is not *res judicata* of the policy coverage question in the Federal court proceedings. Notwithstanding this, the *Fields* court indicated the doctrine of collateral estoppel might apply in a proper case. However, a review of this doctrine demonstrates it is inapplicable in the present case. The *Fields* court said:

> "Notwithstanding this, the doctrine of collateral estoppel applies in a proper case. This doctrine is that the insurer is bound by any material *finding of fact* essential to the judgment of tort liability, which is also decisive of the question of the coverage of the policy of insurance. Restatement, Judgments 293, §68. . . .
>
> "Restatement, Judgments 309, §68, states the rules as follows:
>
> " 'The rules . . . [regarding collateral estoppel] are applicable only where the facts determined are essential to the judgment. Where . . . the court makes findings of fact but the judgment is not dependent upon these findings, they are not conclusive between the parties in a subsequent action based upon a different cause of action.'
>
> "2 Black on Judgments (2nd ed.) 928, §611, states the rule as follows:
>
> " 'The rule has always been regarded as well settled, from the earliest authorities down to the present time, that the judgment, . . . is not conclusive of any matter which was incidentally cognizable in that action, or which came collaterally in question, nor of any matter to be inferred by argument and construction from the judgment. "The estoppel of a judgment extends only to the question directly involved in the issue, and not to any incidental or collateral matter, though it may have arisen and been passed upon.'
>
> "As to what facts are material, 2 Black on Judgments 938, §615, says:

> " 'A judgment is conclusive by way of estoppel only as to facts without the existence and proof or admission of which it could not have been rendered. . . . it is conclusive evidence of whatever it was necessary for the jury to have found in order to warrant the verdict in the former action, and no further.' " 259 P.2d at 640.

In the *Fields* case, the Washington court concluded, based on the above-quoted rules, that the finding that Fields was in the car was material because liability was based on the doctrines of *respondent superior*, and agency, and that no other fact in the findings had even a remote bearing upon those doctrines. In contrast, in the State court action by Kienle, the only *facts* essential to the judgment against Pacific Farwest was that it delivered the deed in violation of the sellers' instructions. The characterization of Pacific Farwest's conduct as "negligence" rather than as simply a breach of the escrow contract was not "essential" to the judgment.[7] Certainly, the judgment could have been rendered without a "finding" of negligence. Thus, the finding of negligence is not determinative of the policy coverage issue, and not binding on appellee.

7. How *non*-essential to the judgment of liability against Pacific Farwest was the formal "finding" of negligence is indicated by the following: no negligence, error or omission on the part of Pacific Farwest was alleged by Kienle in either the original or amended complaints which, rather, alleged a breach of contract. (Ex. 3; Ex. A-20); in the State court litigation appellant's counsel argued to the trial judge that Pacific Farwest breached its contract (Ex. A-29; Tr. 209), and in his oral opinion, the State court judge so held (Ex. A-29 p. 6; Tr. 209). It is instructive to note that the language of Findings of Fact V in the state court action (Ex. 4; Tr. 20) was admittedly drafted by appellants' present counsel (Finding 39, R. 259), and was most likely so drafted for the sole purpose of forming a predicate for collection of the judgment from Pacific Farwest's errors and omissions insurer, the language of whose policy appellants and/or their counsel knew at the time the Findings were drafted. We do not contend impropriety on the part of appellants' counsel in so doing; however, we do contend that this boot-strap effort to establish liability on the part of the insurer, who was not a party to the prior action, must be held ineffectual.

This court, in determining whether or not the conduct of Pacific Farwest in releasing the deed, under all the unique attendant circumstances, constituted a "negligent act, error or omission," may approach this issue *ab initio*, with no assist from the language of the findings entered in the prior state court action.

2. The conduct of Pacific Farwest in releasing the deed, in conscious violation of the Kienles' instructions, was a wilful business decision, and did not constitute a negligent act, error or omission under the escrow policy.

(a) *Conduct of Pacific Farwest.* The evidence supports the District court's conclusion of law that the act of the assured, Pacific Farwest, in releasing the fulfillment deed from escrow, was an intentional and wilful act and did not constitute a "neglegent act, error or omission" within the meaning of the coverage provisions of appellee's policy of insurance. Pacific Farwest had been instructed in writing by two separate attorneys representing Kienle, not to release the deed from escrow. Pacific Farwest consulted its attorney, Mr. Yates, who recommended interpleader, an alternative expressly permitted under the escrow instructions, and characterized as "a fool proof alternative" by appellants' brief at page 22. Notwithstanding this advice, Mr. Cooke, president of Pacific Farwest, decided to deliver the deed, and obtained a written indemnity agreement from Northwestern, two promissory notes, each in amount of $1,500 (one of which was paid) and a mortgage to protect Pacific Farwest in the event of litigation. Cooke knew, prior to the time the deed was released, that there was a "distinct possibility" that Pa-

cific Farwest would be sued if the deed was released.[8]

Thus, as the District court found, Pacific Farwest and its chief officer, Mr. Cooke, knew and fully appreciated that there was a likelihood of being sued if the deed was delivered, but Pacific Farwest nevertheless intentionally and wilfully delivered the deed from escrow (Finding 20; R. 254). The issue then presented is whether or not this conduct constituted a negligent act, error or omission under the policy.

(b) *Policy Coverage is limited to negligent conduct.* The policy covers "negligent act, error or omission." It covers liability caused by negligence alone. Under standard principles of construction and use of the English language, the adjective "negligent" modifies all three of the triad of nouns following it, so the phrase is to be read as if it said "negligent act, negligent error, or negligent omission." A *Grammar of the English Language in Three Volumes, Vol. III, Syntax,* by George O. Curme, pp. 68, 69. In his section entitled "Repetition of Limiting Adjective," on page 68, Dr. Curme states the following rule which is directly applicable to the policy phrase involved in this case:

> "If the limiting adjective modifies two nouns, both representing the same person or thing, or parts of a

8. Cooke's motivation in his calculated decision to release the deed is not made entirely clear by the record. Was it because, quixotically, he believed that Northwestern had complied with its contract with appellants and was entitled to the deed and that under the escrow instructions he had a right to release the deed. (Tr. 193)? Or was it because Northwestern was his best customer, having given him a dozen escrows to handle in less than a year (Tr. 162)? Or was it simply because he considered the fifteen hundred dollars cash Northwestern paid him, plus a promissory note for another $1,500 in the event Pacific Farwest was sued, plus a formal written indemnity agreement, a sufficient *quid pro quo* for his violation of the seller's instructions not to release the deed?

> whole, it should be used only once; while, on the other hand, if the nouns represent different persons or things that it is desired to contrast or to mark as distinct and separate, the limiting adjective should be repeated before each noun. . . ."

The three nouns "act, error or omission" are all "parts of a whole" and belong together for they all refer to something the assured has done or not done which forms the basis of a claim against him which the policy insures. Hence, the limiting adjective "negligent" modifies all three of them.

(c) *The conduct of Pacific Farwest was not negligent.* A review of Washington decisions clearly indicates that Pacific Farwest's act of delivery of the deed, under all the facts here in evidence, did not constitute negligence. In *Adkisson v. Seattle,* 42 Wn.2d 676, 258 P.2d 461 (1953), the court said:

> "Wilful or wanton misconduct is not, properly speaking, within the meaning of the term 'negligence'. *Negligence and wilfulness imply radically different mental states. Negligence conveys the idea of neglect or inadvertence, as distinguished from premeditation or formed intention. An act into which knowledge of danger and wilfulness enter is not negligence of any degree, but is wilful misconduct. As long as the element of inadvertence remains in conduct, it is not properly regarded as wilful.* Wanton misconduct is positive in nature, while mere negligence is materially negative. A person properly chargeable with wanton misconduct is not simply one who is more careless than one who is merely negligent. Wanton misconduct is such as puts the actor in the class with the wilful doer of wrong. 38 Am. Jur. 692 Negligence, §48". 258 P.2d at 465. (Emphasis added.)

Similarly, in *Town of Tieton v. Gen. Ins. Co.,* 61 Wn.2d 716, 380 P.2d 127 (1963), suit was commenced on a

liability policy insuring the Town against legal liability for damages caused by accident. The Town constructed a sewage lagoon which contaminated an adjoining landowner's well and the landowner recovered judgment against the Town. The lagoon was constructed and operated in precisely the manner planned, expected, desired and intended, although the Town did not intend that it should contaminate the well. However, the evidence showed that the possibility of contamination was fully appreciated by the assured and all concerned, but that the Town decided to assume the risk of damage to the well because it was the only location possible to construct the lagoon. The Town had two choices: make a prior settlement with the landowner or proceed with the construction and wait to see if contamination occurred. The court said:

> "The Town officials deliberately chose the latter course and proceeded with construction of the lagoon. This meant that they necessarily had to accept whatever hazard existed that the Town might damage the Pugsby property as a result of the construction. . . ." 380 P.2d at 130.

The trial court held that the damage was caused by accident within the meaning of the policy because the results of the Town's intentional conduct were unanticipated. The Supreme Court disagreed, and held no coverage under the policy in language which we submit is fully applicable to the case at bar:

> "*The evidence most favorable to respondent suggests no more than a finding that respondent took a calculated business risk* that the Pugsby property could not be damaged. From a business standpoint, it may have been wise to have taken this calculated risk. . . . But when, under the facts of this case, the possi-

> bility of contamination became a reality, it cannot be said that the result was 'unusual, unexpected, and unforeseen' ". 380 P.2d at 130-1. (Emphasis added.)

Admittedly the policy in *Town of Tieton* insured against liability caused by accident and the instant policy does not, but the case indicates the Washington court would regard Pacific Farwest's intentional gamble and calculated business risk as constituting the antithesis of neglect or inadvertence which is required for conduct to constitute negligence. *Adkisson v. Seattle, supra.* Nor is it necessary, as appellents suggest, that the actor intend, in a subjective sense, that harm should result to the third party in order for his act to be removed from the category of negligence and become wilful conduct. It is only necessary that he intend the natural and probable consequences of his act. The case at bar is even stronger than the *Town of Tieton* case. Whereas, the Town did not intend to contaminate Pugsby's well and did not know as a certainty that it would be contaminated, Pacific Farwest fully intended and knew that delivery of the deed would complete the conveyance of Kienles' title with whatever damaging consequences to Kienle that would naturally flow from investing Northwestern with record title (Finding 20; R. 254).

The distinction between a negligent act and an intentional act, in the determination of an insurer's liability, was also recognized by this court in *Standard Marine Ins. Co. v. Nome Beach L. & T. Co.,* 133 Fed. 636 (9th Cir. 1904). This was a suit on a marine cargo policy for damage caused as a result of the vessel's sailing through an ice field. The court stated the facts, and the conclusions to coverage to be drawn from such facts, as follows:

> "It appears, however, from the testimony of the master himself, that he well knew of the existence of the ice and of the risk incurred in endeavoring to push through it, and that he well knew all of this in ample time to have avoided it. Can it be properly held that it was not his duty to have avoided the danger—that he did not commit a wrongful act when he deliberately, willfully, undertook to 'fight' his way, as he himself expressed it, through the ice, for the purpose of arriving quickly at Nome, and this secure for his principals a better price for the merchandise, and that they might the sooner realize the profits expected to accrue from the lighterage plant that he carried? We think this must be answered in the negative. Taking the captain's testimony to be true, *it is not, in our opinion, a case of negligence at all whether simple or gross, but one of a deliberate and reckless assumption of a well-known danger, which the law made it the master's duty to have avoided.* It was both a willful omission to perform his legal duty, and an intentional commission of a wrongful act, resulting in the loss in question, for which, both upon principle and authority, the insurer, in our opinion, is not liable." 133 Fed. at 646-7 (Emphasis added.)

In further explanation of the distinction the court said:

> "Negligence and willfulness are the opposites of each other. . . . Negligence is also to be carefully distinguished from fraud; the distinction arising in this case, as before, upon the element of inadvertence. Fraud is invariably intentional, either actually or constructively; negligence is never so * * * An intent to do a wrongful act or to omit the performance of a duty is necessarily willful. Such willfulness may fall short of fraud. . . . 133 Fed. at 647-8.

(d) *The conduct of Pacific Farwest was not an "error" or "omission" within policy coverage.* Pacific Farwest's liability concededly arose out of its wrongful *act* in releasing the fulfillment deed from escrow. Clearly only "negligent" acts are insured, and if as we contend, this

act was not negligent within the policy meaning and hence not covered, it would seem anomalous to hold the same conduct covered by the policy because it constituted an "error." Such an interpretation would ignore the limited adjective "negligent" in the subject policy which modified "act, error or omission."

However, even assuming negligent modifies only the word "act," the conduct of Pacific Farwest did not constitute an "error" or "omission" so as to come within the policy coverage. In *Simon Warrender Prop. Ltd. v. Swain,* (1960) 2 Lloyd's List L.R. 111, suit was brought on an insurance broker's errors and omissions policy insuring against "neglect, omission or error." An employee of the insured brokerage company wilfully failed to effect a policy of insurance on a fishing vessel owned by one Williamson, who sued the company for his loss, and the company having paid, made claim against underwriters. The issue before the court was whether the wilful and deliberate nature of the employee's failure to effect the insurance was a good defense under the policy. The court held that the intent of the employee would not be imputed to the company under the facts of that case, but by necessary implication we believe the court also held that losses resulting from the deliberate acts of the assured, or officers whose acts are necessarily those of an insured corporation, are not within the coverage of such a policy. The *Swain* court stated:

> "But as the plea also alleges that the failure to effect the policy was wilful and deliberate, it is essential to determine whether the words of indemnity embrace such a failure.
>
> "It is clear that in their primary sense both the words 'error' and 'omission' denote conduct which

> is not intentional or deliberate. . . .All these words show that 'the policy deals rather with leaving undone the things one ought to have done rather than with doing things which one ought not to have done'." Id. at 115.

The ground of distinction relied on by the court in the *Swain* case to invoke policy coverage is not present in the case at bar, because Pacific Farwest acted through its president, whose intentional decision, with appreciation of the hazards of litigation, is necessarily attributable to the assured.

The case of *Whitworth v. Hoskin*, (1939) 65 Lloyd's List L.R. 48, a decision of the Mayor's and City of London's Court, also supports appellee's position. One Frith, an accountant, was insured by Lloyd's under an indemnity policy insuring against claims "in respect of any act of neglect, default or error." One Kirby, who used Frith's office and facilities with his consent, defrauded plaintiff, who thereafter recovered judgment against Frith. Plaintiff then sued Frith's errors and omissions underwriters as assignee. The *Hoskin* court said:

> "Then it is said that 'he held out Kirby as his representative and as a person entitled to receive money on behalf of the vendor or James Frith & Co.' The answer of Mr. Soskice to that is that 'that was not a 'neglect' or an 'error.' It is quite clear from Frith's evidence that it was what he intended to do and what he did do. There was no neglect about it at all and there was no error.' As to that, of course, that is the matter, in a way, that the judgment was suffered in respect of, but it does not, to my mind, come within the terms of this policy.
>
> "*On the cases cited to me, I think it is quite clear that that is not the sort of act which can be described as a 'neglect' of 'error,' that is, when a man is doing*

exactly what he intends to do, even if he may be wrong in doing it." Id. at 50. (Emphasis added.)

Similarly, in *Haseldine v. Hoskin*, (1933) 45 Lloyd's List L.R. 59, a solicitor was sued for bringing a lawsuit under a contingent fee agreement and posting costs for his client, an illegal practice though the solicitor was not aware of the illegality. The solicitor settled the suit and sought indemnity from Lloyd's underwriters. The court held no coverage, first because the act on which the solicitor's liability was based was illegal, and second, because it was not within the policy coverage entirely apart from the illegality. Lord Justice Slesser stated:

> "Lastly, I am unable to see that there was any loss sustained here by an 'neglect, omission or error.' The loss sustained here is the result of an action brought because this gentleman, Mr. Haseldine, financed and assisted in an action, thereby causing damages to Messrs. Sterms, damages which were originally stated as special damage to amount to the sum of £2811 and which he subsequently compromised for a considerably smaller sum. *I am unable to say that this loss was caused by an error. It was caused by Mr. Haseldine entering into an agreement; that agreement was not entered into in error; It was done deliberately by him for the purposes recited in the agreement. He may or may not have mistaken the legal effect of what he was doing, but it is wrong in my opinion to say that the loss was occasioned by error.* The loss was occasioned by the agreement." Id. at 67.

Thus, it must be concluded that Pacific Farwest's delivery of the deed was not a "negligent act, error or omission" within the policy coverage. No reasonable construction of the policy requires appellee to underwrite the failure of the assured's intentional business gamble under the circumstances of this case.

3. Appellant's authorities do not support their contention that the conduct of Pacific Farwest constituted a negligent act, error or omission under the escrow policy.

Appellant's place primary reliance upon *Sutherland v. Fid. & Cas. Co.*, 103 Wash. 583, 175 Pac. 187 (1918). In *Sutherland*, a physician contracted with a patient to remove all of his gallstones and all cause of disease possible to be removed by a surgical operation. The physician failed to find the offending gallstone, which failure was the basis of his liability to the patient.[9] The physician sued on his malpractice policy insuring him against "loss from liability imposed by law" on account of bodily injury suffered in consequence of "malpractice, error or mistake" in the practice of his profession. Although the physician recovered, the case is clearly not in point. Rather, the case involved a simple case of negligence rather than the kind of intentional conduct which appellants seek to bring within the policy coverage.

Similarly, in *Brown v. Underwriters at Lloyd's*, 53 Wn. 2d 142, 332 P.2d 228 (1958), a real estate broker was held liable because the court said he was careless in not making an investigation as to the truth of the owner's statement before passing it on to the buyer of property involved in a sale. There was no eveidence that the broker knew the statement to be false.

Two California cases, also relied upon by appellants, are equally not in point. In *Russ-Field Corp. v. Underwriters at Lloyd's*, 164 Cal. App.2d 83, 330 P.2d 432

9. It affirmatively appears from the reported opinion in the suit by the patient against the physician, *Schuster v. Sutherland*, 92 Wash. 135, 158 Pac. 730 (1916), that the physician simply missed the gallstone.

(1958), a motion picture producer's policy covered claims for negligent act, error or omission and for breach of contract. The producer settled an action alleging breach of contract in making changes in a script, and then sued underwriters on the policy. The distinguishing features of that case are evident from the language of the court's opinion, immediately following appellant's quote at page 33 of their brief, as follows:

> "The finding that the breach, if one occurred, was not 'wilful' is supported by substantial evidence. Mr. Tatelman testified in substance that he made arrangements for filming from the revised screenplay on the assumption that Mr. Genn would play his role in the revised version without objection. It is a legitimate inference that when Mr. Genn's objections were made known, it was too late to do anything but proceed to produce the film on the revised version." 330 P.2d at 440.

Similarly, in *Aitchison v. Founders Ins. Co.*, 166 Cal. App.2d 432, 333 P.2d 178 (1959), the insured's liability was based upon his certificate that the ore he sold to the government was of domestic origin, but he did so in good faith *without knowledge* that the ore had been smuggled into the country.

Appellants can find no authority to support their position that the policy insures the kind of intentional business risk undertaken by Pacific Farwest, and therefore rely upon shopworn contention that the policy should be liberally construed in favor of the insured. However, contrary to the implication of appellants, in construing insurance policies, the Supreme Court of Washington does not avidly seize upon every element of doubt so as to create an ambiguity and then construe it against the insurer so as to permit recovery by the insured. Rather, the court ad-

heres to the concept that the polar star of construction of an insurance contract is the intention of the parties. *Boeing Etc. Co. v. Fireman's Etc. Co.*, 44 Wn.2d 488, 268 P.2d 654 (1954); *Gen. Cas. Co. v. Azteca Films, Inc.*, 278 F.2d 161 (9th Cir. 1960). Coverage is clearly limited to claims made against the assured "by reason of any negligent act, error or omission." The absense of an express exclusion concerning intentional acts is not necessary in light of the plain and unambiguous scope of policy coverage. Notwithstanding this fact, and contrary to appellants' assertion, appellee does not urge, and this court need not hold, that every intentional act is beyond policy coverage. Undoubtedly there are circumstances where the act, though intentional, would nonetheless be classed as negligence. An example is *Bancroft v. Indem. Ins. Co.*, 203 F. Supp. 49 (W.D. La. 1962), cited by appellants on page 34 of their brief. There the insured accountant deliberately and intentionally issued an opinion to a client that a proposed stock transfer would be nontaxable. He was wrong and the court held his resulting liability to the client was covered by his professional liability policy covering "neglect, error or omission." But as the accountant's testimony clearly showed (203 F. Supp. 52), in his research he simply missed section 304 of the 1954 Internal Revenue Code. Thus, no sweeping generalization that the policy does not cover any intentional act of the assured is required in order to uphold the judgment of the court below.

Appellants ask, what does this policy cover if it does not cover a legal liability incurred as a result of an escrow transaction? It certainly covers more than liability from an upset ink bottle obliterating a signature. *Citizens Nat.*

Bank v. Davisson, 229 U.S. 212, 57 L.2d. 1153 (1913) furnishes an example. There a depositary returned money to the buyer on a real estate contract without checking the provisions of the contract, in reliance on an incomplete memorandum of the conditions written on an envelope containing the contract. The Supreme Court held this was a negligent omission; this would have been covered by an errors and omissions policy. Counsel for appellee have handled for Underwriters at Lloyds a number of claims against escrow agents which reasonably would come within the protection of the policy. These include a claim based on the escrow agent's failure to obtain an acknowledgment on an option for extension of a lease of real property, invalidating the extension under the statute of frauds; and a claim based on the escrow agent's negligent failure to record a second mortgage which caused damage to the mortgagee when he lost his priority. Appellee's policy is not illusory and the protection afforded not a sham. But compare these examples and those in the cases cited by appellants with the facts of the instant case: the escrow agent not only intentionally violated the instructions of the seller not to deliver the deed, but he sold his violation of instructions to the buyer for $1,500. This conduct was a wilful act not within any reasonable construction of the protection which underwriters took to furnish by the policy.

This is not a case where the State legislature has required an automobile owner to maintian libility insurance for the protection of the public. The only relevant public policy to this case is the requirement that an escrow agent maintain a fidelity bond for fidelity coverage. There is no requirement that liability insurance be maintained, and

Pacific Farwest was not required to carry errors and omissions insurance. It must follow that appellants have no standing to complain, as against appellee, that the policy which Pacific Farwest did in fact carry was vitiated by the acts of Pacific Farwest.

If underwiriters are held to have insured Pacific Farwest in these circumstances, they in effect become partners in the escrow business with Pacific Farwest, and their insurance policy becomes a surety bond. No rule of liberal construction of insurance policies in favor of insureds and against underwriters, so as to "effectuate desirable social purposes" either compels or justifies this result.

D. The Findings of Fact Entered by the District Court Specified as Error, are Fully Supported by the Evidence.

Findings of Fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses. Rule 52(a), Federal Rules of Civil Procedure, 28 U.S.C.A. The Federal courts have frequently stressed the importance of the trial judge's advantage to see and hear the witnesses as they testify. *Orvis v. Higgins,* 180 F.2d 537 (2nd Cir. 1950), cert. denied, 340 U.S. 810, 95 L.ed. 595 (1950). The weight to be given to the specific finding, will, of course, depend upon the character of the evidence.

1. Finding of Fact 20

Appellants specify error to the use of the word "likelihood" in Finding of Fact 20 (R. 254). This finding that Pacific Farwest knew and fully appreciated that there was a likelihood of being sued, under all the circumstances,

is based largely on the oral testimony of Mr. DeCrane Cooke, President of Pacific Farwest. Cooke testified that he clearly understood there was a "distinct possibility" that Pacific Farwest would be sued in the event he released the fulfillment deed to Northwestern (Tr. 175). Cooke further testified that in order to secure Pacific Farwest in the event of litigation, Pacific Farwest obtained the indemnity agreement, two demand promissory notes and mortgage from Northwestern (Tr. 170, 175, 175, 180, 202-204). These facts, based on Cooke's testimony, completely supports this finding. Though appellants contend that the last sentence of Finding 20, "the delivery of the deed did not constitute a negligent act, error or omission," is a conclusion of law and not a finding of fact, this court ordinarily regards a trial court's determination that a party is or is not negligent as a finding of fact, subject to the "clearly erroneous" rule of review on appeal. *Pacific Tow Boat Co. v. States Marine Corp.*, 276 F.2d 745 (9th Cir. 1960).

2. Finding of Fact 22

Appellants specify error to the court's finding that the original complaint in State court charged Pacific Farwest with fraud and did not allege a claim within appellee's policy. This contention has been fully refuted heretofore in the brief (Appellee's Brief, pp. 13-16). This finding is based on the original complaint and the policy of insurance, both documents in evidence, and is clearly correct (Ex. 1; Ex. A-20).

3. Finding of Fact 30

Appellants object to the second portion of Finding 30 (P. 257) on the ground that the forwarding of the amend-

ed complaint by the assured, when requested by appellee's counsel, was not a condition precedent and further that appellee had not made sufficient effort to obtain the documents. Whether the requirement of the policy is a condition precedent is clearly a question of law and this subject has heretofore been discussed (Appellee's Brief, pp. 31-33). Whatever burden is placed upon the insurer to obtain the cooperation of the insured in such matters as attending trial, the authorities cited by appellants do *not* impose upon an insurer an affirmative obligation to solicit tender of defense or solicit proper notice of claim, of which forwarding the suit papers is an essential. The policy puts this obligation on the assured, not the underwriters. Finally, the testimony of Mr. Yates, clearly established that his determination not to furnish the pleadings, documents and information requested was purposeful and hence was intentional (Tr. 85, 94-5).

4. Findings of Fact 31, 32 and 33

Appellants except to all but the first sentence of Finding 31 and all of Findings 32 and 33, on the grounds that the Findings deal with matters which took place subsequent to the trial of the State court action and that these Findings are allegedly in sharp conflict with the testimony. The Findings are fully supported by the testimony of witness Moss (Tr. 73-74), established by the documentary evidence admitted in the case (Ex. A-27, Tr. 97; Ex. A-28, Tr. 97), and not denied by assured's counsel Yates. And although the events occurred after the trial of the State court action had been concluded, they evidenced the continuing breach by the assured of the cooperation clause of the policy and the facts are therefore both material and relevant. Appellee submits that had

assured's counsel Yates furnished the documents requested, and responded to Exhibit A-28 concerning prospective appeal, underwriters might well have determined to finance an appeal rather than await the present suit on the policy. However, the assured's continued non-cooperation made these alternatives impossible.

5. Finding of Fact 41

Appellants specify error to Finding 41 that appellants did not prove by a preponderance of the evidence that Pacific Farwest's delivery of the deed was a violation of legal duty owed to appellants. Appellants had signed bilateral escrow instructions and had not revoked them. They had no right to instruct the escrow agent not to deliver the deed unless the purchaser, Northwestern, had not complied with its obligations under the master real estate contract. In the court below appellants did not prove that the purchaser had not complied and thus did not prove that Pacific Farwest was not within its rights as escrow holder in releasing the deed. Further, no evidence of any kind was introduced relating to the amount of damages, even assuming liability was established.

E. The District Court Correctly Denied Appellants' Motion for Summary Judgment

Prior to trial, cross motions for summary judgments were presented to the District court. Appellee submits that based on the agreed facts in the pre-trial order, the District court was correct in denying appellants' motion for summary judgment, but erred in denying appellee's motion for summary judgment. However, the District court wished to try the case on its merits with full evidence. The refusal to pass on the motions for a summary judgment was within the sound discretion of the court, and is

not reversible error. *Woods v. Robb,* 171 F.2d 539 (5th Cir. 1948).

V.

CONCLUSION

When insureds or their judgment creditors have little law to support them, they invariably urge considerations of public policy, social justice and the time-honored cry of "ambiguity," in their attempts to recover against an insurer. This case is no exception, and appellants ask this court to reverse the judgment below not so much because the law compels it, but rather because this court, as an instrument of social justice, should abhor the thought that the appellants' plight should befall anyone and that one be without recourse." (App. Br., p. 69). Because the assured here used the words "Bonded and Insured" at the bottom of its stationery, appellants say that appellee must pay the loss as a matter of social justice, despite the obvious fact that no court has ever suggested that a representation that one is insured is tantamount to a representation that all legal liabilities are covered by such insurance. Similarly, there is no evidence whatever in the record to support appellants' suggestions that appellee and its counsel were motivated by the Machiavellian considerations ascribed to them, so as to produce a "synthetic defense." The trial court certainly made no such finding, and we suggest that this court should respectfully decline to substitute imagined motivation for facts and law in determining the issues of this case. This court sits as a court of legal review, not as an instrument of social justice whose function is to spread the loss so that no one member of the public shall have to bear it.

The District court correctly concluded that appellee was not bound by the State court judgment of liability against Pacific Farwest. There is no legal authority to support appellants' contention that appellee should have solicited a tender of defense from Pacific Farwest at the risk of being bound by the State court judgment. The District court was also correct in holding that the assured breached an express condition precedent of the policy when it intentionally failed to furnish the amended complaint at the request of the insurer, because the policy placed the burden on the assured to give notice and furnish information. Finally, the District court was correct in holding that the assured's intentional business gamble, with full appreciation of the risk which resulted in the liability judgment against it, was not the kind of conduct insured by the escrow errors and omissions policy here in issue.

If sound principles of law be substituted for sympathy for appellants' plight, the judgment of the court below was correct and must be affirmed.

Respectfully submitted,

LANE, POWELL, MOSS & MILLER
THOMAS S. ZILLY
Attorneys for Appellee

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with these rules.

THOMAS S. ZILLY
Of Attorneys for Appellee

APPENDIX A

PLAINTIFFS' EXHIBITS

No.	Document	Page of Transcript where Offered	Admitted
1.	Certificate of Insurance.	16	18
2.	Judgment & Decree, Cause No. 630 691.	18	19
3.	Amended Complaint, Cause No. 630 691.	19	19
4.	Findings & Conclusions of Law No. 630 691.	20	20
5.	Letter from Jeremiah M. McCormick to Gordon W. Moss, dated May 20, 1965.	21	21
7.	Letter dated December 1, 1964 to Wood Ins. from Pacific Farwest Mortgage & Escrow	21	21
8.	Letter dated May 26, 1964 to Howard R. Kienle from Pacific Farwest Mortgage & Escrow	27	29
9.	Letter dated 12/5/1964, to Voigt-Walker & Co. from Wood Ins. Co.	105	106

DEFENDANTS' EXHIBITS

No.	Document	Page of Transcript where Offered	Admitted
A- 2.	Sellers' Escrow Instruction	148	149
A- 7.	Letter dated July 17, 1964 from attorney Gouge to Pacific Farwest.	142	146
A- 8.	Letter dated July 23, 1964 from attorney Carpenter to Pacific Farwest	142	146

DEFENDANTS' EXHIBITS (Continued)

No.	Document	Page of Transcript where Offered	Admitted
A- 9.	Letter dated 7/28/64 from attorney Youngberg to DeCrane Cooke of Pacific Farwest	164	165
A-13.	Mortgage to Pacific Farwest from Northwestern Utilities, dated 8/18/64.	176	177
A-19.	Letter dated Aug. 20, 1964, from Pacific Farwest to Fidelity Savings & Loan Assn.	178	179
A-20.	Complaint, Cause No. 630 691.	67	70
A-21.	Copy of letter from Yates & Yates, dated 12/7/64 to Voigt-Walker & Co.	67	70
A-22.	Letter from Gordon W. Moss, dated 2/15/65 to Yates & Yates	60	60
A-26.	Letter from Gordon W. Moss, dated 2/24/65 to Yates & Yates	61	63
A-27.	Letter from Gordon W. Moss, dated 12/1/65 to Leslie M. Yates	95	97
A-28.	Letter from Gordon W. Moss, dated 5/18/66 to Leslie M. Yates.	95	97
A-29.	Oral Opinion, Cause No. 630 691.	206	209
A-30.	Original Indemnity Agreement	201	202
A-31.	Promissory Note dated 8/19/64	203	204

APPENDIX B

INDEMNITY AGREEMENT

THIS AGTEEMENT, entered into this 18th day of August, 1964, between NORTHWESTERN UTILITIES, INCORPORATED, a Washington corporation, WILLIAM A. CANNON and MELVIN D. FREIMUTH, individually, hereafter called Indemnitors and PACIFIC FAR WEST MORTGAGE AND ESCROW COMPANY, a Washington corporation, DE CRANE COOKE and CYRIL H. DYE, hereafter called Indemnitees,

WITNESSETH:

WHEREAS, Indemnitees are closing in escrow a certain real estate transaction between Northwestern Utilities, Incorporated, as Purchaser, and Howard R. Kienle and Dora Joy Kienle, his wife, as sellers, pursuant to a real estate contract entered into between the parties and executed April 12, 1964, and

WHEREAS, Northwestern Utilities, Incorporated, has fully performed as Purchaser its obligations in escrow, including the tender of certain real estate contracts to said Kienles to secure the fulfillment or warranty deed held in escrow and

WHEREAS, Northwestern Utilities, Incorporated, has demanded of Indemnitees that said fulfillment or warranty deed executed by said Kienles to Northwestern Utilities, Incorporated, be filed and the escrow closed and

WHEREAS, the Indemnitors have agreed to indemnify the Indemnitees and to hold said Indemnitees harmless from any and all future suits, claims or demands of any nature against said Indemnitee arising out of the closing of said escrow.

Now, Therefore, in consideration of the delivery by Indemnitees of said deed, Indemnitors do hereby jointly and severally agree that they will at all times hereafter indemnify Indemnitees and each of them against any loss, damage, suit or expense of any kind or nature which Indemnitees may sustain or incur by reason of the closing of said escrow transaction by the filing of said fulfillment or warranty deed from said Kienles to Northwestern Utilities, Incorporated and as further consideration Indemnitors have on this date, executed two promissory notes to Indemnitees secured by certain assets of Indemnitors. One note is a demand note for $1,500.00. The other is for $1,500.00 payable in the event suit is commenced as a result of the release of the said deed. As to the cash indemnity, Indemnitees have the right to keep a portion of said funds in payment of such expenses as they have incurred to this date and will incur in the future. Such expenses will include, but will not be limited to, attorney's fees, time loss of Indemnitees or any of them and such other loss and in such amounts as Indemnitees may deterine in their sole discretion.

In Witness Whereof, the parties hereto hereunder set their hands and seals the day and year first above written.

Northwestern Utilities, Incorporated
Northwestern Utilities, Inc.

By William A. Cannon,
William A. Cannon, President

Melvin D. Freimuth, Secretary
Melvin D. Freimuth, Secretary

William A. Cannon, Individually
William A. Cannon, Individually

MELVIN D. FREIMUTH, Individually
MELVIN D. FREIMUTH, Individually

PACIFIC FAR WEST MORTGAGE & ESCROW CO.
PACIFIC FAR WEST MORTGAGE & ESCROW CO. INC.

By DE CRANE COOKE, President
DE CRANE COOKE, President

CYRIL H. DYE, Secretary-Treasurer
CYRIL H. DYE, Secretary-Treasurer

DE CRANE COOKE
DE CRANE COOKE, Individually

CYRIL H. DYE
CYRIL H. DYE, Individually

APPENDIX C

May 24, 1965

Messrs. Yates & Yates
Attorneys at Law
Suite 203, 1800 Westlake Ave. North
Seattle, Washington 98109

Attention: Leslie M. Yates

Re: *Kienle v. Pacific Farwest Mortgage & Escrow Co., Inc., et al*—
Cause 630691—Our File 26097

Dear Sirs:

We enclose copy of letter received from Attorney McCormick. Please furnish us a copy of all relevant pleadings subsequent to the original complaint and answer, including particularly the amended complaint. Advise also the current status of Pacific Farwest Mortgage & Escrow Co., Inc. and whether you intend to continue to defend your client in this case.

We have never been provided with a copy of the earnest money receipt and agreement, the real estate contract, or the escrow instructions and would appreciate your furnishing us a copy of the same; if there were no written escrow instructions please advise.

Underwriters continue to reserve all rights under the applicable Errors & Omissions Certificate.

Yours very truly,

EVANS, MCLAREN, LANE, POWELL & MOSS
ss/Gordon W. Moss

GWM:AM
enc.
2cc Voigt, Walker & Co., Inc.